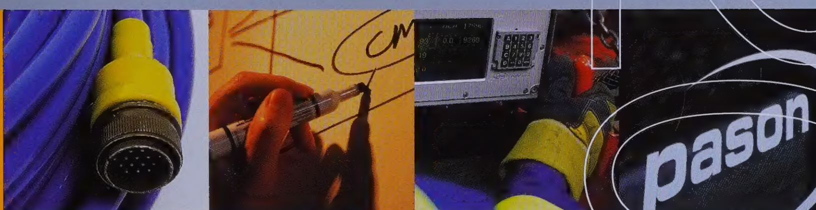
PASON SYSTEMS INC. \ ANNUAL REPORT

2001



At Pason, our goal is to deliver the integrated wellsite instrumentation and data solutions our customers need.


pason

EDR


pason
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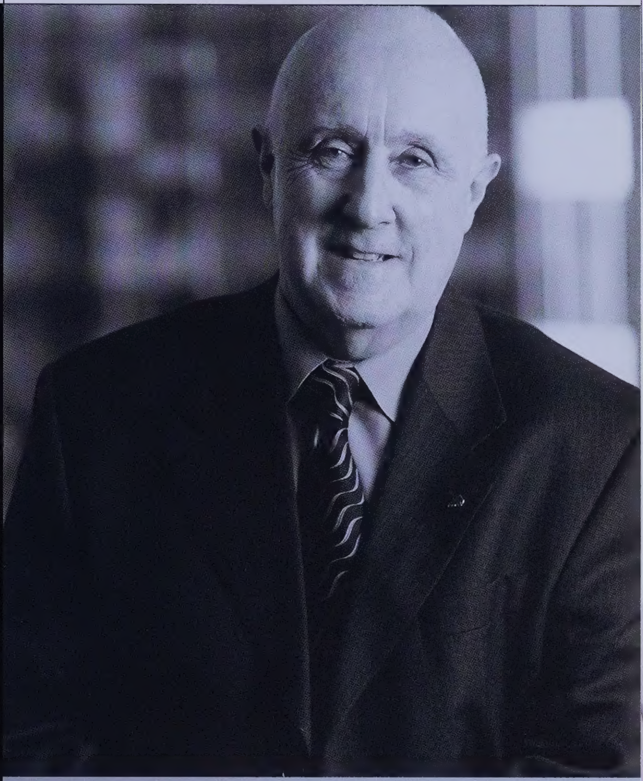
Pason PENLESS
pason
TECH SUPPORT:
1-877-255-3158
J-BOX
TOOL-PUSH
KEYPAD

◂ ELECTRONIC DRILLING RECORDER

PASON'S ELECTRONIC DRILLING RECORDER (EDR) IS A COMPLETE SYSTEM OF INSTRUMENTATION AND MONITORING EQUIPMENT THAT ACTS AS A BASE FOR ALL DATA CAPTURE, DATA DISPLAY AND COMMUNICATIONS AT THE DRILLING WELLSITE. EACH EDR SYSTEM CONSISTS OF A PROPRIETARY INDUSTRIAL COMPUTER, SENSOR SET AND JUNCTION BOX, TOGETHER WITH A SERIES OF WORKSTATIONS CONNECTED VIA A LOCAL AREA NETWORK IN ORDER TO SHARE REAL-TIME DRILLING INFORMATION WITH ALL WELLSITE PERSONNEL. THE PASON EDR PROVIDES COMPREHENSIVE INFORMATION WITH EASE OF USE AND RELIABILITY, MAKING IT THE ENVY OF THE INDUSTRY AND THE CORNERSTONE TO WHICH ALL SUBSEQUENT PASON PRODUCT OFFERINGS ARE LEVERAGED.

Denis J. Reid

NORTHERN CONTRACTS & JOINT VENTURES ADMINISTRATOR
AKITA DRILLING LTD. – CALGARY, ALBERTA



We at Akita Drilling pride ourselves on providing quality services to our customers, which includes an exemplary safety record and the willingness to adopt proven technologies. Pason has played a strategic role within our company since 1990, and today we use Pason equipment on most of our 36 rigs.

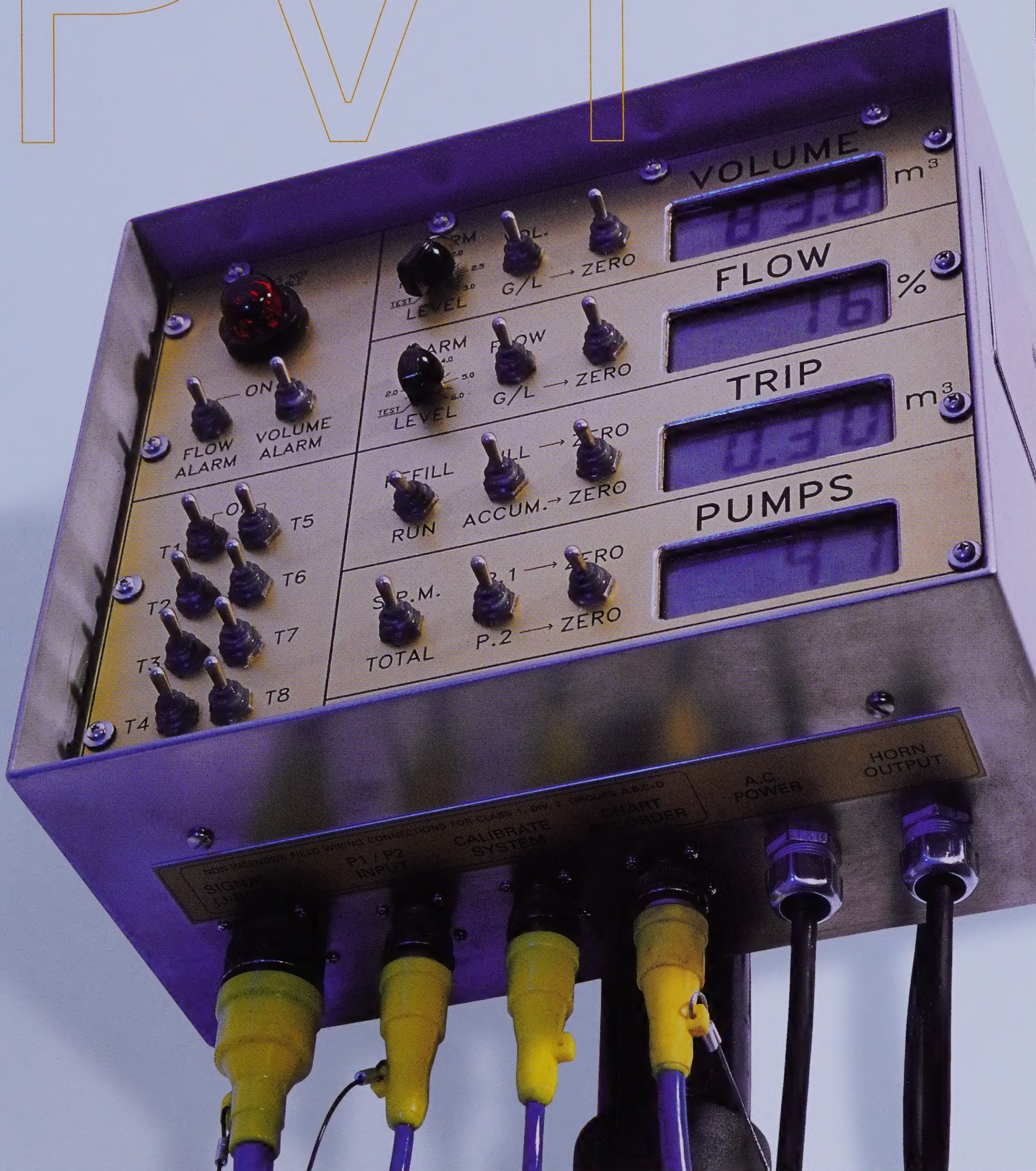
Peter McLelland, P.ENG.
WELL CONTROL SPECIALIST – CALGARY, ALBERTA

The advantage of using Pason electronic data is that it allows for an accurate assessment of wellbore conditions prior to a well control operation. From that point on, off-site personnel can provide assistance to the wellsite supervisor in regaining control. The acquisition of volume data using the Pason Pit Volume Totalizer during the control operation facilitates a team approach, further improving the safety and success of the operation.

PIT VOLUME TOTALIZER ▸

THE PIT VOLUME TOTALIZER (PVT) IS PASON'S PROPRIETARY SOLUTION FOR THE DETECTION AND EARLY WARNING OF "KICKS" THAT ARE CAUSED BY HYDROCARBONS ENTERING THE WELLBORE UNDER HIGH PRESSURE AND EXPANDING AS THEY MIGRATE TO THE SURFACE. OPERATING IN CONJUNCTION WITH THE COMPANY'S ELECTRONIC DRILLING RECORDER, PASON'S PVT IS ACKNOWLEDGED AS THE LEADER IN FUNCTIONALITY, RELIABILITY AND EASE OF USE, AND IS AN ESSENTIAL SAFETY ADDITION TO ALL DRILLING OPERATIONS.

PVT


VOLUME
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G/L → ZERO
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G/L → ZERO
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m3
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ALARM
VOLUME
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RUN
ACCUM.→ ZERO
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TOTAL
P.2 → ZERO
T5
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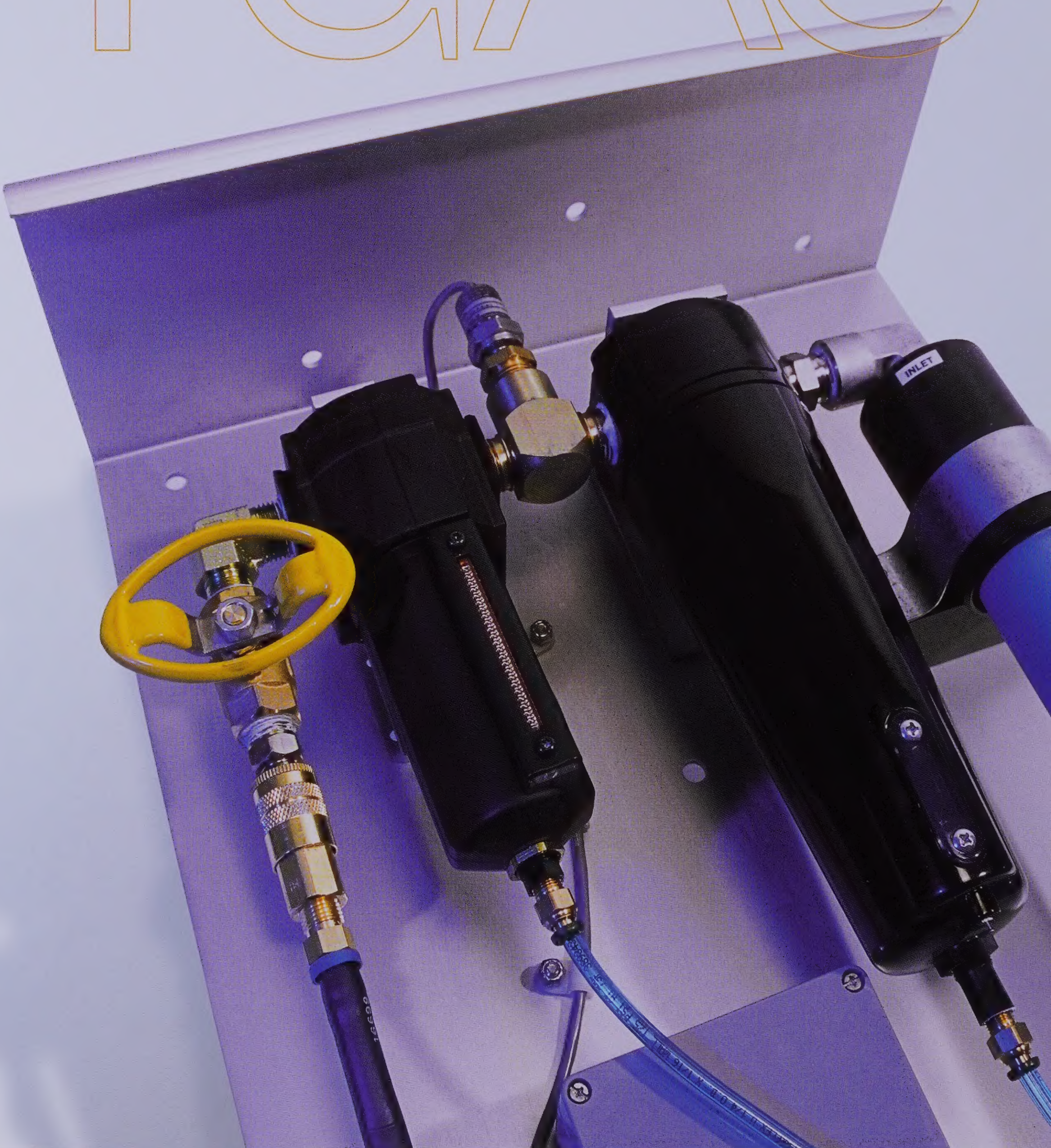
T4
CALIBRATE
SYSTEM
A.C.
POWER
HORN
OUTPUT

TGAS



Andy Wolff
SENIOR GEOLOGIST
EL PASO OIL & GAS CANADA, INC. – CALGARY, ALBERTA

◂ TOTAL GAS SYSTEM

TOTAL GAS SYSTEMS (TGAS) MEASURE THE TOTAL HYDROCARBON GASES (C1 THROUGH C5) EXITING THE WELLBORE AND THEN CALCULATE THE LAG TIME TO SHOW THE FORMATION DEPTH WHERE THE GASES WERE PRODUCED. A ROBUST SYSTEM CAPABLE OF OPERATING WITH A HIGH DEGREE OF ACCURACY, PASON'S TGAS PROVIDES THE MAXIMUM AMOUNT OF INFORMATION WITH THE MINIMUM AMOUNT OF MAINTENANCE IN THE MOST EXTREME OF ENVIRONMENTAL CONDITIONS. THIS SYSTEM IS DESIGNED TO OPERATE WITH PASON'S ELECTRONIC DRILLING RECORDER AND AS SUCH, THE INFORMATION IT PROVIDES CAN BE VIEWED BY ANY WELLSITE USER VIA THE DATA NETWORK.

The Pason Total Gas System is uniquely designed to address the inherent problems in conventional gas detection units. It is a low maintenance, easy-to-use system that accurately analyzes the relative gas readings within the mud column. I am impressed with Pason's novel approach and use of technology to provide us with consistent and reliable gas analysis.

Brad K. Virginillo

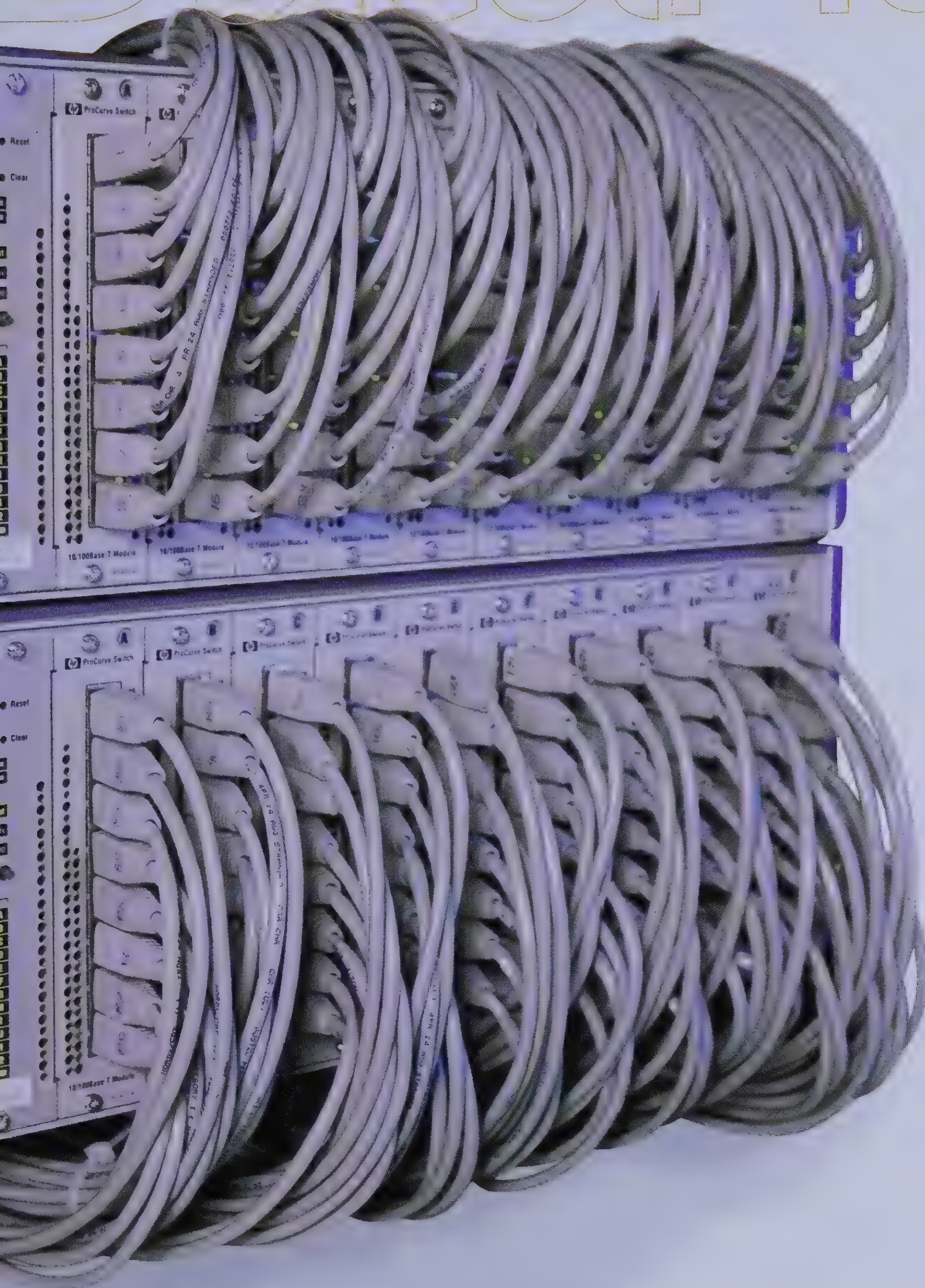
DRILLING ENGINEERING MANAGER
ANADARKO CANADA CORPORATION – CALGARY, ALBERTA

Anadarko is one of the largest independent oil and gas exploration and production companies in the world, with activities in 16 countries. In Canada, Pason provides us with reliable service for electronic recording and transmission of our drilling rig data through their Internet DataHub. The Pason DataHub has become an important link in our data flow from the rig to the office. Well information is collected and then viewed at the rig site in real-time and in almost real-time in our office, providing for more accurate, timely data that assists us in making quicker and better informed drilling decisions.

INTERNET DATAHUB ▸

THE PASON INTERNET DATAHUB PROVIDES A CONVENIENT AND INEXPENSIVE MECHANISM TO COLLECT AND STORE FINANCIAL AND DRILLING ENGINEERING DATA IN A TRUE ELECTRONIC WELL FILE. THIS WELLSITE DATA IS THEN DISSEMINATED AND RETRIEVED BY OPERATOR PARTNERS AND SERVICE CONTRACTORS FROM ANY LOCATION THAT HAS INTERNET ACCESS, ALLOWING THEM TO MONITOR THE PROGRESS OF DRILLING OPERATIONS, PROVIDE ASSISTANCE WHERE APPROPRIATE AND IMPROVE OVERALL DRILLING EFFICIENCY. THIS PRODUCT PROVIDES THE IDEAL PLATFORM FROM WHICH TO MARKET NEW PASON SERVICES TO THE COMMUNITY OF DRILLING USERS WHO ALREADY REGULARLY VISIT THE DATAHUB SITE.

DataHub



WebPay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Pason Systems Inc
ABC Oil
Wild Rose Creek
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Jeff Sal[illegible]

DRILLING MANAGER

CAZA DRILLING INC. – DENVER, COLORADO

WEBPAY

THE UPSTREAM OIL AND GAS INDUSTRY SPENDS IN EXCESS OF $15 BILLION IN CANADA AND $100 BILLION WORLDWIDE ON THE PROCUREMENT AND PAYMENT OF DRILLING GOODS AND SERVICES. THE GREATEST ADMINISTRATIVE COST TO THE INDUSTRY IS IN TRACKING THESE GOODS AND SERVICES AT THE WELLSITE, AUTHORIZATIONS FOR PAYMENT AND PHYSICAL PROCESSING OF A DELUGE OF PAPER INVOICES FROM THOUSANDS OF DIVERSE SUPPLIERS. THROUGH ITS DOMINANT WELLSITE POSITION, RIG DATA NETWORK AND INTERNET DATAHUB, PASON HAS DEVELOPED WEBPAY, ITS PAPERLESS INVOICE APPROVAL SYSTEM WITH AUTOMATIC CHARGE CREATION AND RAPID APPROVAL PROCESS. WEBPAY OFFERS SIGNIFICANT TIMESAVING FOR DRILLING MANAGEMENT PERSONNEL; TIME THAT IS BETTER SPENT ON OPTIMIZING DRILLING PERFORMANCE.

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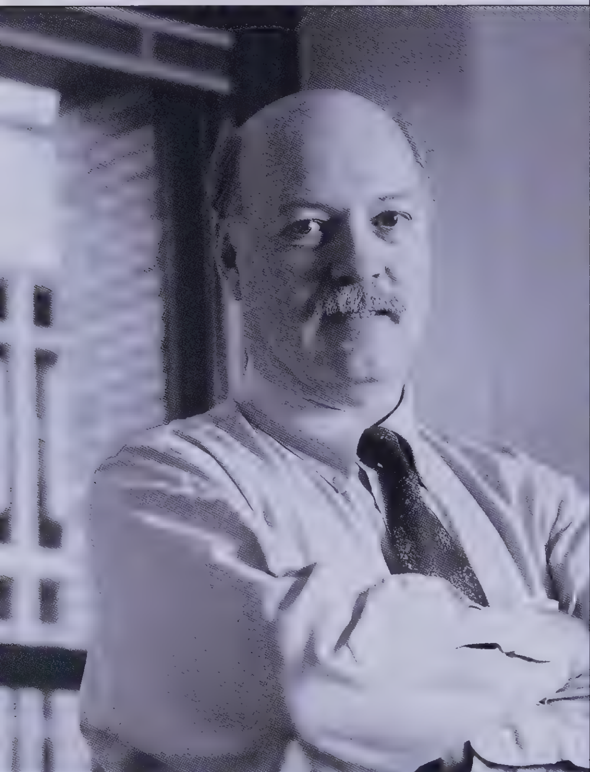
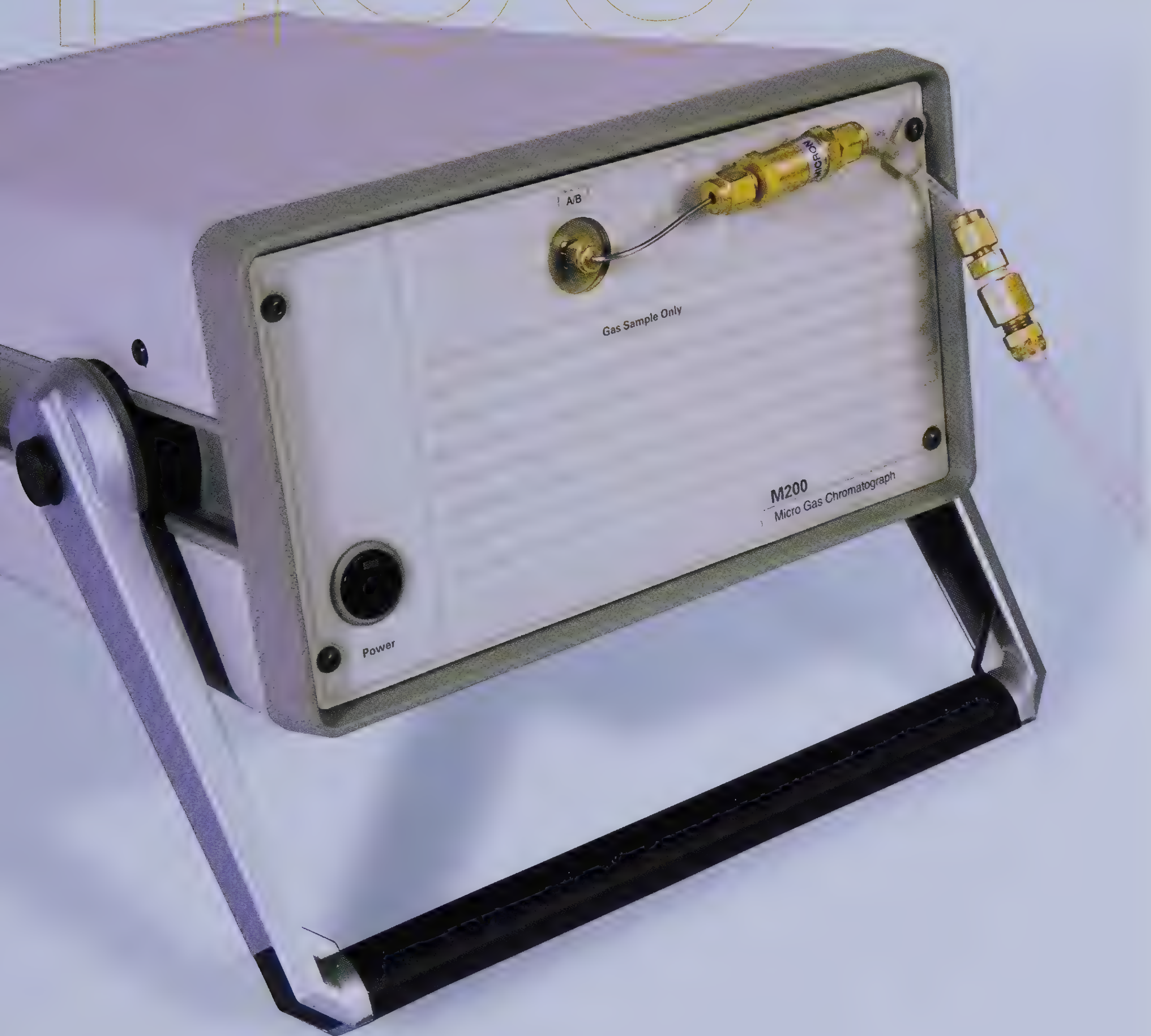
Fletcher S. Walters
EXPLORATION MANAGER, ROCKY MOUNTAINS
YATES PETROLEUM CORPORATION – DENVER, COLORADO



HIGH-SPEED CHROMATOGRAPH ▸

IN THE UNITED STATES, PASON PROVIDES COMPLETE MUDLOGGING AND SUBSURFACE GEOLOGICAL CONSULTING SERVICES. PASON'S WELLSITE GEOLOGISTS AND MUDLOGGING TECHNICIANS ARE EQUIPPED WITH SPECIALIZED INSTRUMENTS SUCH AS THE HIGH-SPEED CHROMATOGRAPH (HSC) TO MONITOR THE GAS IN DRILLING RETURNS AS WELL AS PICK FORMATION TOPS AND ANALYZE DRILLING CUTTINGS. THE HSC IS SPECIFICALLY DESIGNED FOR ACCURATE GAS SAMPLE (C1 THROUGH C5 AND CO_2) ANALYSIS IN LESS THAN 30 SECONDS. THE DETAILED DATA PROVIDED BY THE HSC IS USED IN GEO-STEERING OF HORIZONTAL WELLS AND IN RATIO PLOTS TO HELP IDENTIFY RESERVOIR FLUIDS.

HSC



field services

Robert L. Hemsing
PRESIDENT
HEMSING DRILLING LTD. – CALGARY, ALBERTA

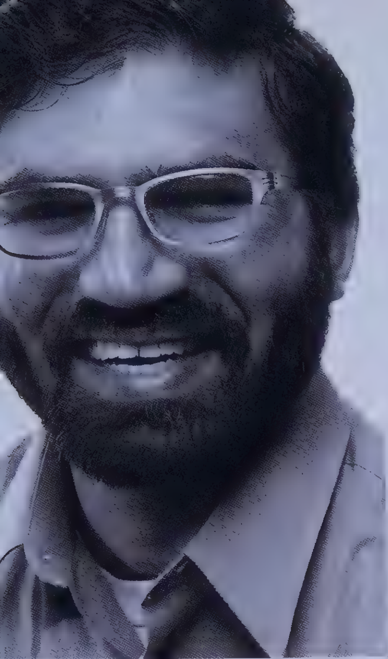
FIELD SERVICES

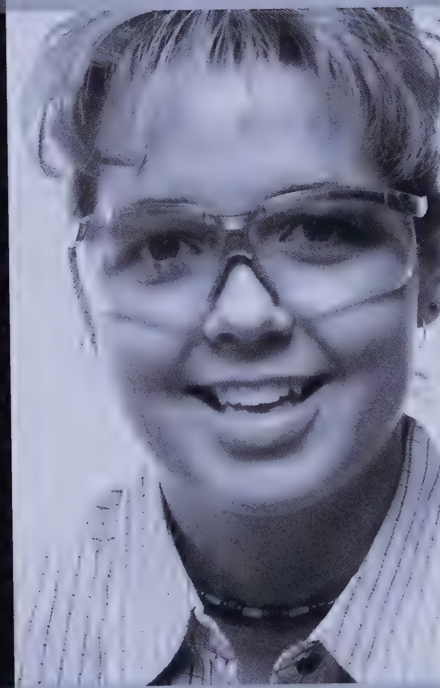
PASON IS COMMITTED TO MAINTAINING ITS REPUTATION FOR INDUSTRY BEST SERVICE AT THE WELLSITE. PASON'S FIELD STRUCTURE IS UNIQUE TO THE OILFIELD SERVICE INDUSTRY IN THAT ITS SERVICE TECHNICIANS ARE BASED OUT OF THEIR HOMES, WHICH ARE LOCATED IN CLOSE PROXIMITY TO RIG SITES. TO PASON CUSTOMERS, THIS TRANSLATES INTO RAPID RESPONSE TIMES – TYPICALLY WITHIN THE HOUR – COMPARED TO TRADITIONAL SERVICE COMPANY STRUCTURES THAT WOULD REQUIRE A ONE WAY, FOUR TO SIX-HOUR DRIVE TO THE SITE. EACH PASON FIELD SERVICE TECHNICIAN IS ON CALL 24/7 AND OUTFITTED WITH ENOUGH EQUIPMENT FOR A NEW SYSTEM INSTALL. IN ADDITION TO INITIAL EQUIPMENT INSTALLATION AND SETUP, SERVICE TECHNICIANS PROVIDE ON-SITE EQUIPMENT TRAINING AND MAINTENANCE.

customer

Pason staffs a 24/7 toll free technical help desk to provide our customers with immediate advice to help solve their hardware or software issues.

PASON'S FLEET OF RENTAL INSTRUMENTATION GROWS PRIMARILY THROUGH RECOMMENDATIONS FROM SATISFIED WELLSITE CUSTOMERS. IN RECOGNITION OF THIS, PASON HAS INVESTED HEAVILY TO ENSURE THAT EACH CUSTOMER RECEIVES THE BEST POSSIBLE EXPERIENCE WHEN USING PASON EQUIPMENT. WE HAVE MADE IT THE PRIMARY RESPONSIBILITY OF EACH PASON EMPLOYEE, WHETHER IN THE FIELD OR IN THE OFFICE, TO PROVIDE THE INDUSTRY BEST IN CUSTOMER CARE.






pason

Corporate Profile

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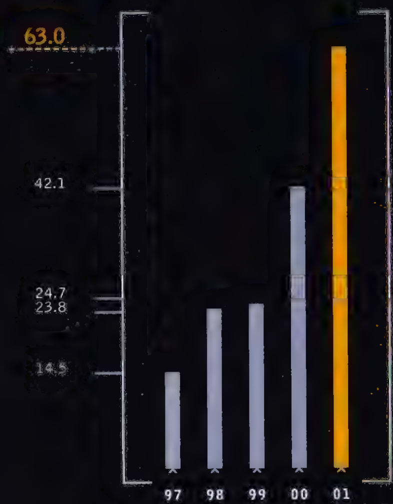
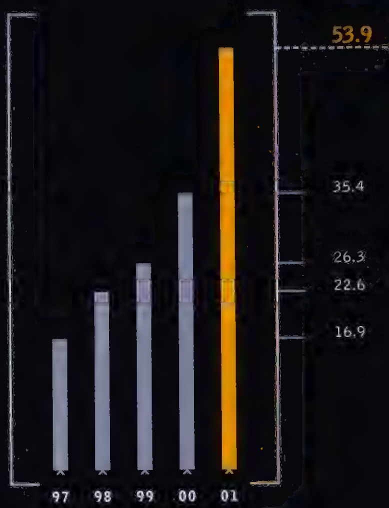


REVENUE
($millions)



SHAREHOLDERS' EQUITY
($millions)

RETURN ON EQUITY
(%)

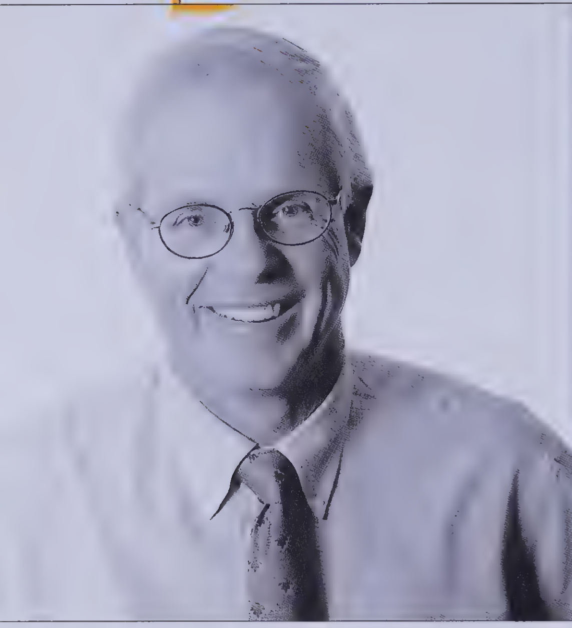
MARKET CAPITALIZATION
($millions)

Years Ended December 31,	2001	2000	Change
	$	$	%
Revenue	**63,016,000**	42,144,000	50
Net earnings	**15,437,000**	8,117,000	90
Per share – basic	**0.90**	0.49	84
Per share – diluted	**0.88**	0.47	87
Cash flow from operations	**24,941,000**	14,797,000	69
Per share – basic	**1.45**	0.89	63
Per share – diluted	**1.42**	0.85	67
EBITDA	**35,396,000**	20,797,000	70
Per share – basic	**2.06**	1.25	65
Per share – diluted	**2.02**	1.20	68
Capital expenditures	**22,921,000**	23,419,000	(2)
Working capital	**5,135,000**	1,416,000	263
Total assets	**82,252,000**	64,451,000	28
Shareholders' equity	**53,941,000**	35,448,000	52
Return on shareholders' equity	**35%**	26%	35
Market capitalization at year-end	**159,000,000**	117,000,000	36
Weighted average shares outstanding	**17,147,210**	16,603,965	3

Quarterly Results

2001	**Q1**	**Q2**	**Q3**	**Q4**
	$	**$**	**$**	**$**
Revenue	**17,052,000**	**12,712,000**	**17,543,000**	**15,709,000**
Net earnings	**4,796,000**	**2,350,000**	**4,682,000**	**3,609,000**
Per share – basic	**0.29**	**0.13**	**0.27**	**0.21**
Cash flow from operations	**6,620,000**	**4,354,000**	**7,130,000**	**6,837,000**
Per share – basic	**0.39**	**0.26**	**0.41**	**0.39**

2000	Q1	Q2	Q3	Q4
	$	$	$	$
Revenue	10,698,000	7,538,000	10,802,000	13,106,000
Net earnings	2,675,000	997,000	1,951,000	2,494,000
Per share – basic	0.16	0.06	0.12	0.15
Cash flow from operations	4,380,000	1,586,000	4,807,000	4,024,000
Per share – basic	0.27	0.10	0.29	0.23



We are dedicated to integrating our specialties into comprehensive wellsite instrumentation and data solutions that are designed to deliver superior returns for our customers, our company and our shareholders. We excel at recognizing what our customers need and that knowledge becomes our bridge between vision and reality.

JIM HILL – PRESIDENT & CHIEF EXECUTIVE OFFICER

Results for the Year

For the sixth consecutive year, we are pleased to report record revenues, with significant year-over-year financial gains in all areas.

- INCREASED REVENUE 50% TO $63.0 MILLION.
- GREW NET EARNINGS 90% TO $15.4 MILLION OR $0.90 PER SHARE.
- IMPROVED OPERATING CASH FLOW 69% TO $24.9 MILLION OR $1.45 PER SHARE.
- INCREASED EBITDA 70% TO $35.4 MILLION OR $2.06 PER SHARE.
- STRENGTHENED SHAREHOLDERS' EQUITY A FURTHER 52% TO $53.9 MILLION.

At Pason, we pride ourselves on being more than a cyclical oilfield services company that experiences gains in years of strong commodity prices and losses during periods of downturn. Our consistent financial growth certainly bears testimony to this claim. In a 2001 survey of 1,000 Canadian public companies conducted by Canada's leading financial newspaper, Pason was ranked #18 based on return on equity over the previous five years. With a 35% return on equity in 2001, we should remain one of Canada's leading companies in this category.

Growing Our Business

Pason provides a tightly integrated package of products including drilling data acquisition, wellsite reporting software, remote communications and Internet data storage and management. Although our strategy for growth is simple, the execution is much more difficult. WE CONTINUE TO SEEK INCREASES IN BOTH THE NUMBER OF SITES AT WHICH WE PROVIDE OUR PRODUCTS AS WELL AS THE NUMBER OF PRODUCTS WE PROVIDE AT EACH SITE.

To that end, during 2001 we continued to increase our dominant Canadian market presence such that by year-end, our core product - the Electronic Drilling Recorder (EDR) - was

installed on an estimated 90% of the active drilling rigs. In the United States, we grew our market share approximately 1% per month for the first six months of the year, following which the U.S. rig count began to seriously decline and at which time our growth also leveled off. Today, Pason products are installed on 20% of the active rigs in that country. During the year, we also established a profitable base of operations in Mexico. Although Pason equipment has been installed on only seven rigs to date, we believe we are the new leader in this emerging market due to our operational structure and the strong support we have gained from the national Mexican oil company, and therefore we look to increase our presence throughout 2002 and beyond. Our experience in Mexico has also allowed us to develop a business template for performing similar rental services in other countries. Our model places Pason as the prime rental company liaising directly with the end customer, while all service is performed by a local service provider that is then compensated with a fixed percentage of the gross rents. This arrangement offers an incentive for the local service provider to operate as efficiently as possible while sheltering Pason from the risks of unexpected losses often associated with foreign operations.

A key metric for Pason is how much rental product revenue we generate for each drilling day logged in the industry. ALTHOUGH PASON'S 2001 REVENUE PER DAY INCREASED IN BOTH CANADA AND THE U.S., MORE SIGNIFICANT WAS THE FACT THAT OUR CANADIAN NUMBERS IMPROVED 21% TO $298 PER DAY. This was achieved despite maintaining our product prices and the modest 10% increase in the number of rigs on which Pason's equipment was installed. THIS CLEARLY INDICATES OUR SUCCESS IN INCREASING SITE REVENUE THROUGH THE ADDITION OF COMPLEMENTARY PRODUCTS. Our new Electronic Choke and Total Gas Systems, although still early in their commercial lives, are already positively affecting our per site revenue.

Pason's products operate in two ways: in the field to provide data acquisition and control capabilities, and in the office (primarily using the Internet) to provide data storage and retrieval in order to facilitate management of field operations. As the Pason Internet DataHub continues to mature, more drilling managers are seeing the benefits of this "drilling cockpit". Although to date it does not generate its own revenue stream, it certainly drives additional EDR rentals. As a larger drilling community starts to actively use this site, the potential for a new revenue stream should evolve. In parallel to the DataHub, we continue to develop our Internet-based oilfield invoice approval system - WebPay - and if successful, we see this software product generating its own revenues by the end of this fiscal year. With these two products, the wellsite's operational and financial data streams can be merged, eliminating significant duplication of effort. To most customers, the e-commerce market remains fragmented and confusing, which has certainly slowed our progress in gaining acceptance of our vision for WebPay. As a result, we are purposely keeping a low marketing profile during its initiation, thereby allowing us to conserve resources while we continue to actively develop the product's features with the assistance of a U.S. drilling contractor. We anticipate that as market confusion clears, we will be ready with a robust and well-tested system that will gain acceptance from skeptical and risk averse customers.

THE TWO PILLARS OF PASON'S COMPETITIVE ADVANTAGE ARE ITS FIELD SERVICE STRUCTURE AND ITS TECHNOLOGY. The expansion of our business has allowed us to devote significantly more resources to continuously develop both of these two crucial components. The effort expended in bringing all North American field service technicians to our Calgary facilities for training and development under the Pason service culture, has allowed us to maintain industry best

service despite the rapid increase in the number of sites we service. Further, during the year we made major improvements to our systems for managing the many complex R&D projects that we are concurrently developing. As a result, I am even more confident that as we go forward, we will effectively utilize and benefit from our increasing resources.

Outlook

The exploration and development drilling budgets of our customers (the market for our services) have been reduced due to the lower prices for oil and natural gas that they received in the latter half of 2001. However, we take comfort in the fact that the oil and gas industry is a true "free market", unfettered by subsidies and marketing boards, and as a result, normal market forces work swiftly to reduce any imbalance between supply and demand. This summer, U.S. natural gas production is expected to be down 5% from the prior year while demand, encouraged by lower prices, should increase 5%. Consequently, we still expect commodity prices to strengthen by late 2002, giving rise to another surge in drilling activity.

GIVEN THE INCREASING RESOURCES OF PASON, WE ARE CONFIDENT WE WILL CONTINUE TO FIND WAYS TO GROW IN ANY STAGE OF OUR CYCLICAL INDUSTRY. As more North American customers take on new international drilling assignments, we are receiving increased requests for tendering our services in their new markets. Our successful expansion into Mexico gives us confidence to actively pursue these new opportunities as we move forward. We are also considering the possibilities for our products on drilling rigs outside of the oil and gas industry, further extending our market beyond its current limits.

Our industry may be cyclical but we are committed to positive, consistent growth. For their valuable contributions towards that goal this past year, I thank all of our employees and directors.

On behalf of the Board of Directors,

JD Hill

JIM HILL
PRESIDENT & CHIEF EXECUTIVE OFFICER

April 4, 2002


CMR

RENTAL REVENUE PER INDUSTRY DRILLING DAY
($)

In 2001, revenue per North American industry drilling day increased an average 22%. Pason believes that the cummulative daily rental value of its current products and those in development could generate an economic package in excess of $700 per drilling day.

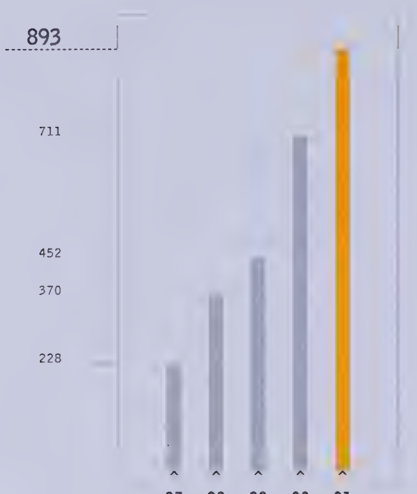
Rental Instrumentation

PASON DESIGNS, MANUFACTURES AND DELIVERS AN INTEGRATED PACKAGE OF RENTAL PRODUCTS THAT OFFER WELLSITE DATA ACQUISITION AND DRILLING MANAGEMENT BENEFITS AT BOTH THE RIG SITE AND IN THE OFFICE. During 2001, revenues generated by instrumentation rentals totaled $53.6 million compared to $35.1 million a year ago. In addition, the gross margin achieved from its rental products remained steady at 75% compared to 74% recorded in 2000.

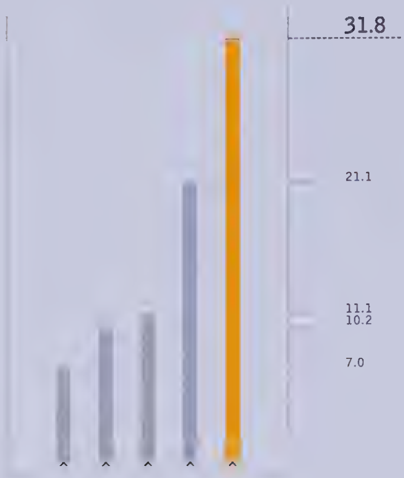
The Pason Electronic Drilling Recorder (EDR), and its existing infrastructure, serves as the cornerstone to which all subsequent product offerings are leveraged. The development of the Company's Canadian and U.S. rental product revenue per industry drilling day is outlined below:

	Industry Drilling Days	Pason Rental Revenue	Revenue Per Day
	#	$	$
Canada			
1997	128,000	12,400,000	97
1998	89,400	14,800,000	166
1999	81,800	15,000,000	183
2000	117,400	29,000,000	247
2001	**120,400**	**35,900,000**	**298**
United States			
1998	258,400	3,300,000	13
1999	191,600	4,200,000	22
2000	281,400	7,500,000	27
2001	**354,400**	**17,300,000**	**49**

Pason believes that the cumulative daily rental value of its current data acquisition, control and data management products as well as those in development, could generate an economic package in excess of $700 per drilling day. The progress made over the past five years in Canada indicates that the Company is well on its way to meet this goal. Although daily rental revenue in the U.S. is still miniscule in comparison, more impressive is the fact that 2001 rental revenues from this market have already exceeded Canadian revenues posted as recently as 1999.



EDR SYSTEMS
(systems at year-end)



EDR REVENUE
($millions)

ELECTRONIC DRILLING RECORDERS

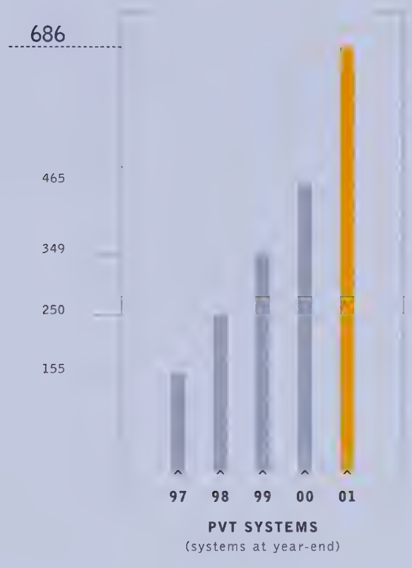
The Company was largely able to meet all requests for its EDR during 2001, and with the decline in drilling activity late in the year, initiated a corresponding reduction in new builds. By the end of 2001, Pason's electronic data acquisition instrumentation had been installed on an estimated 90% of the active Canadian rigs and on 20% of the active U.S. rigs, thereby generating revenue of $31.8 million compared to $21.1 million the prior year. Pason continues to invest heavily in upgrading its EDR fleet such that each unit is equipped with all of the features customers require. Over the course of the past 12 months, network speed at the rig has been significantly improved, and as a result, the Company is currently enhancing its software to allow its EDRs to take advantage of the broad band Internet access expected to be economically viable and available at most wellsites by the end of 2002.

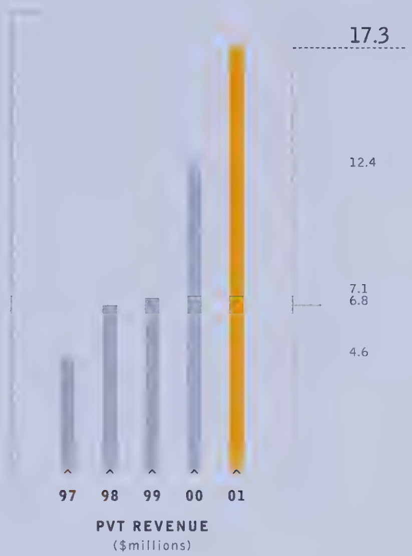
PIT VOLUME TOTALIZERS

The Pason Pit Volume Totalizer (PVT) remains the industry's tool of choice as evidenced by another strong year of revenue growth – a 40% increase to $17.3 million. Canadian drilling regulations now allow operators to reduce surface casing depth when a PVT is employed, thereby justifying the use of this instrument on practically every well. Currently, Pason PVTs have been installed on 90% of Canadian and 63% of U.S. rigs on which it has an EDR system.

TOTAL GAS SYSTEMS

During 2001, the Pason Total Gas System (TGAS) generated new revenue of over $1.1 million, however these results were below expectations. There were two reasons for this underperformance. The TGAS is extremely complex in design as it seeks to provide a more accurate





gas sample while dramatically reducing daily maintenance requirements. As the Company began to roll out a larger fleet of systems, several moderate design flaws were detected, and although these flaws appear to have been rectified, initial customer acceptance was slowed as a result. The second obstacle encountered was marketing related. Despite the fact that drilling personnel, Pason's traditional customer base, were solidly behind the use of Pason's TGAS, the same could not be said for wellsite geologists with whom Pason had had little previous contact. Through a concentrated marketing effort, however, Pason has been gaining greater acceptance from this new customer group in recent months. Currently, the TGAS is being rented at an annualized value of $2.0 million and growing, and while Pason still believes that its TGAS will dominate the industry, its growth will take longer than originally forecast. Pason's TGAS offers greater versatility compared to competitors' systems and, therefore, has the potential to be used on 75% of Canadian and 50% of U.S. drilling rigs.

ELECTRONIC CHOKE SYSTEMS

All customers employing Pason's new Electronic Choke System are extremely satisfied, and as a result, revenue from this product was up 140% in 2001 to $1.3 million and is expected to double again in 2002. Pason's system, used to control and remove detected gas "kicks" from the wellbore, can be found on approximately 25% of the Canadian rigs in operation. Once again, Pason is pushing a new business model where the choke valve portion of the system becomes the responsibility of the drilling contractor while Pason provides the electronic actuation and display. Although this model provides greater industry safety, it has yet to gain acceptance in the United States and, therefore, to date all revenue for this product has been derived from Canada. The Company still expects to eventually generate significant revenue from its Electronic Choke System in the United States.

Data Management Services

Through its rental products, Pason continues to add value to the data acquired at the wellsite. The Company's vision is to converge all drilling engineering and financial wellsite data together in one Internet site. This site will provide internally developed management tools with broad market appeal plus facilities to download data into more narrowly focused third party specialty applications.

INTERNET DATAHUB

Initially, Pason's Internet DataHub was designed simply to collect data from the rig and act as an incentive to use other Pason products for wellsite data acquisition. That vision has subsequently developed to the point where the DataHub now provides a platform for several new services that will be marketed to the community of drilling users who regularly visit the Pason DataHub site. During 2001, the graphical interface for the site was reworked allowing customers greater display customization of their wells. As broad band Internet access to the rigs becomes more common later in 2002, the Pason Internet DataHub will become even more critical as it will blend both historical and real-time data access. There are currently over 2,000 registered users of this Pason product versus 800 a year ago.

WELLSITE ENGINEERING DATABASES

In addition to sensor data, there is a considerable amount of manual data that must be collected daily by wellsite supervisors. This process has suffered from a number of problems over the years. Firstly, there are numerous suppliers of wellsite engineering database software, with each system having a different look and feel. Secondly, wellsite supervisors generally work as independent contractors for a number of operator customers, and therefore must learn the various software packages. Thirdly, each operator has mobilization problems: they must get their particular software package out to the wellsite for each new well, plus arrange for communications to permit the data to return to their central office database. Finally, even if an engineering database with superior wellsite data entry capability becomes available, most operators cannot change systems because of their investment in supporting the office side of the database.

Pason has been carefully considering this problem, and in 2002 is rolling out an elegant solution to these compatibility and mobilization challenges. Building on the wellsite engineering package developed by Peloton Computer Enterprises, a leading provider of this type of product, Pason will provide a generic engineering database capture module as part of its standard EDR software package. Because this new module will follow the Pason EDR and the rigs on which it works, wellsite supervisors will be more familiar with how to use the software while office drilling superintendents will not be required to make special mobilization efforts for software and communications. Pason will display all data in standard forms on its Internet DataHub; however, should customers require greater analysis or desire to have the information transferred to another supplier's database, data will be available for export from the Pason DataHub using WITSML.

REMOTE LOCATION CHARGE APPROVAL

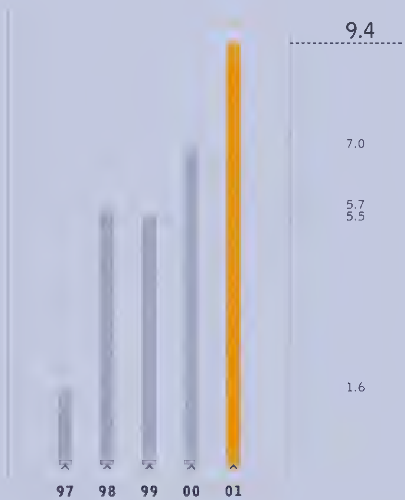
Pason continues to develop a unique solution for the challenges faced in approving charges generated at remote rig sites. The current process has proven to be extremely cumbersome and error-prone for most operator customers, while valuable drilling management time that is better spent on optimizing drilling performance is consumed by routine accounts payable functions.

For the past two years, Pason has been developing its solution, known as WebPay, primarily with a U.S. drilling contractor. This contractor and many of its suppliers are now benefiting from its automatic charge creation, rapid approval and the complete absence of paper. WebPay utilizes Pason's rig presence and EDR for the initial entry point. The Pason Internet DataHub can then combine financial and engineering data, thereby providing an all-encompassing site for complete drilling management. Pason expects to have the product ready for more widespread use by the middle of 2002.

Geological Services

In the United States, the Company provides skilled wellsite geologists and mudlogging technicians to monitor gases in the drilling returns as well as pick formation tops and analyze drilling cuttings. Pason performs this service only in the U.S. market because of the tight link between the geological service provider and the specialized equipment that is used. In Canada, separate companies provide the geological personnel and instrumentation required for each job.

In 2001, Pason achieved record revenues of $9.4 million from its geological services and, more importantly, the gross margin for these services grew to a record 33%, up from 24% in 2000. Pason has been consistently trying to improve the business model for this sector that has traditionally had very low margins.



GEOLOGICAL SERVICES REVENUE
($millions)

Historically, U.S. customers have been presented with two very different options for geological supervision: either do without or incur the significant costs of a dedicated geological service provider on location. For less critical wells in more developed basins, a reduced scope of geological services is required. Using its EDR, TGAS and DataHub products, Pason provides value to customers utilizing geological service providers who simultaneously supervise multiple wells or who provide complete supervision from a remote location. This model, although having the advantage of attracting scarce geological talent while providing the customer with a more economical solution, would not be feasible without Pason's unique suite of integrated instrumentation products.

New Markets

The Company's first serious international operations commenced in May 2001 with its entry into Mexico. Two major oilfield service companies working for the state owned Petroleos Mexicanos (Pemex) under multi-well integrated service contracts in the prolific Burgos Basin of Northern Mexico, selected Pason for their instrumentation needs. Over the seven-month period, Pason rented seven rig instrumentation packages (which included an EDR, PVT and TGAS on each rig) and in each case, service that would typically be provided by Pason field service technicians in Canada and the U.S. was instead provided by a local Mexican company. Pemex has been very pleased with the performance of Pason instrumentation and is currently preparing new multiple services contracts for the Burgos field, which should increase opportunities for Pason instrumentation rentals in 2003.

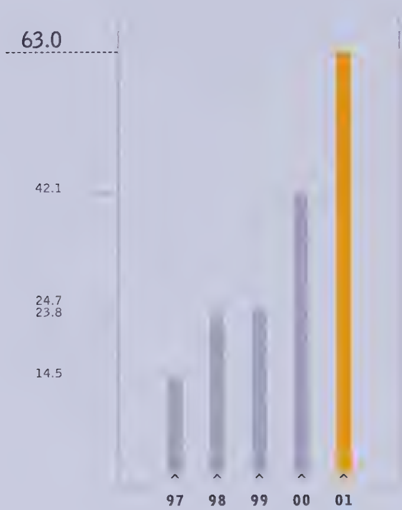
The business model that Pason developed for Mexico, which maintains the Company's ownership of all its equipment while protecting it from unexpected costs associated with local service providers, appears to be solid and of value elsewhere in the world. Accordingly, Pason is now aggressively pushing this model in several Eastern Hemisphere countries.

REVENUE
($millions)

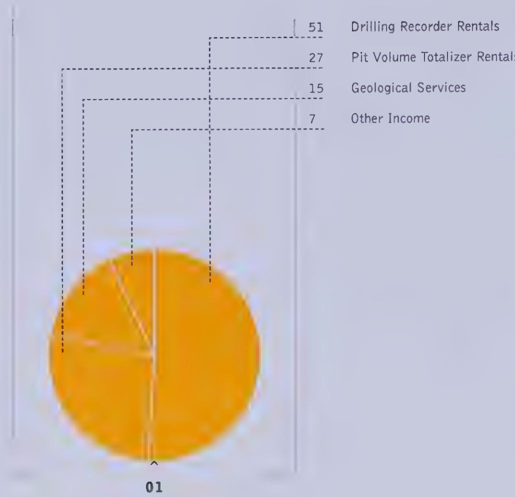
The following discussion and analysis has been prepared by management and is a review of the financial results of the Company based on accounting principles generally accepted in Canada. Its focus is primarily a comparison of the financial performance for the years ended December 31, 2001 and 2000 and should be read in conjunction with the consolidated financial statements and accompanying notes.

Certain information regarding the Company contained herein may constitute forward-looking statements under applicable securities laws. Such statements are subject to known or unknown risks and uncertainties that may cause actual results to differ materially from those anticipated or implied in the forward-looking statements.

Years Ended December 31,	2001	2000	Change
	$	$	%
Revenue			
Drilling recorder rentals	**31,796,000**	21,058,000	51
Pit volume totalizer rentals	**17,317,000**	12,405,000	40
Geological services	**9,404,000**	7,045,000	33
Choke control rentals	**1,292,000**	538,000	140
Total gas rentals	**1,105,000**	–	100
Other income	**2,102,000**	1,098,000	91
Total revenue	**63,016,000**	42,144,000	50
Expenses			
Rental services	**13,641,000**	9,290,000	47
Geological services	**6,262,000**	5,326,000	18
Shop	**2,551,000**	1,899,000	34
Research and development	**2,750,000**	2,006,000	37
Administration	**2,415,000**	2,826,000	(15)
Interest	**1,324,000**	915,000	45
Depreciation and amortization	**7,341,000**	5,340,000	37
Consolidated total expenses	**36,284,000**	27,602,000	31
Net earnings	**15,437,000**	8,117,000	90
Per share – basic	**0.90**	0.49	84
Cash flow from operations	**24,941,000**	14,797,000	69
Per share – basic	**1.45**	0.89	63
Margins			
Rental services	**75%**	74%	1
Geological services	**33%**	24%	38



REVENUE
($millions)



REVENUE MIX
(%)

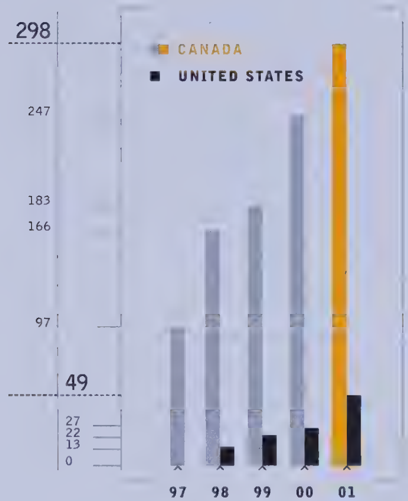
Revenue

Revenue, generated primarily from instrumentation rentals and geological services, increased $20.9 million to $63.0 million in 2001 from $42.1 million the prior year. This 50% improvement was due to increases in the number of rental units and products available along with demand for these units, which was brought about by record North American drilling activity levels experienced in the first nine months. During 2001, Canadian rentals accounted for 57% or $35.9 million of the Company's total revenue, with 42% or $26.7 million coming from U.S. operations and the remaining 1% or $0.4 million generated from Mexico and other international activities. This is compared to 67% or $28.0 million and 33% or $14.1 million recorded in 2000 for Canada and the United States, respectively. The necessary infrastructure over the vast geographical area in the United States to support rentals continues to improve and in part contributed to the U.S.'s strong rate of increase, along with the strength of the U.S. dollar. This market continues to provide significant future opportunities.

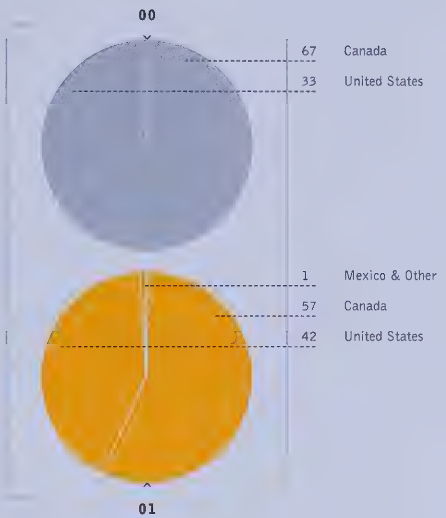
Total Pason rental days for EDRs in Canada were roughly 96,000 in both 2001 and 2000 while the United States recorded 58,000 rental days compared to 32,000 a year ago. PVT rental days totaled 82,000 for the year in Canada versus 65,000 in 2000. PVT rentals in the United States totaled 34,000 compared to 15,000 the prior year. These activity gains parallel the year-over-year revenue gains made in 2001.

Expenses

Over the past two years, expenses incurred by the Company have reflected the cost associated with building an infrastructure to service the dramatically higher activity levels experienced in 2000 and the first nine months of 2001. Accordingly, consolidated total expenses rose 31% or $8.7 million to $36.3 million in 2001 versus $27.6 million the prior year. Over 70% or $6.3 million of this predominantly activity-based increase came from growing rental services expenses and increased depreciation and amortization costs.



RENTAL REVENUE
PER INDUSTRY DRILLING DAY
($)



RENTAL REVENUE
BY GEOGRAPHIC REGION
(%)

During 2001, rental services expenses increased $4.3 million or 47% to total $13.6 million compared to $9.3 million in 2000. These expenses consisted primarily of wages and related benefit costs, which are approximately 50% of rental services expenses for both Canada and the United States, and the additional direct costs of field servicemen, including but not limited to vehicle costs, communication, equipment repairs and freight. As industry activities increased and in order to maintain the highest level of service, the Company continued to recruit and train additional fieldmen. At year-end, there were 66 field service technicians versus 54 at December 31, 2000, a significant contributor to the increase in overall rental services expenses. Also during 2001, Pason commenced operations in Mexico that are conducted through a Mexican service company; however, there were up-front training costs that were included as part of the 2001 rental services expenses.

Geological services expenses rose 18% to $6.3 million from $5.3 million in 2000. The increase was primarily attributable to labour and related costs, which represent over 75% of the total of these expenses compared to 67% in 2000. The rate of increase in geological services expenses (18%) was considerably slower than the rate of geological services revenue (33%), thereby contributing to the improvement in the related margin.

The assembly and distribution of Pason products, which are included in shop expenses, rose 34% from $1.9 million to $2.6 million. Over 50% of the increase was due to growing personnel costs associated with the high levels of activity throughout most of 2001, with the remaining increase attributed to higher freight and shipping costs.

R&D expenses increased 37% in 2001 to $2.7 million from $2.0 million the prior year; however, capitalized R&D decreased 31% from $1.7 million to $1.3 million in 2001. The year's total increase in R&D, expensed and capitalized, was $0.3 million or 8%.

Administrative expenses decreased 15% from $2.8 million to $2.4 million in 2001. A number of one-time charges that occurred in 2000, including the relocation to new premises, were not incurred in 2001.

Interest expense increased 45% from $0.9 million to $1.3 million in 2001. The Company continued to use its credit facilities in both Canada and the U.S. as well as $2.5 million in sales-leaseback financing to fund the manufacture of new rental equipment.

Depreciation and amortization expenses increased 37% to $7.3 million from $5.3 million in 2000. A significant portion of the Company's tangible assets are depreciated using a unit-of-use method of accounting as it best matches revenue and expenses.

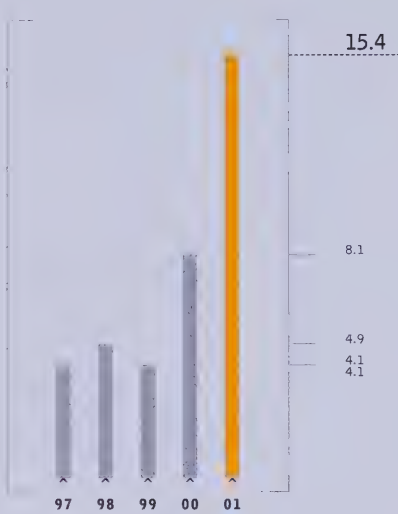
Current income tax expense rose $4.0 million from $5.1 million in 2000 to $9.1 million in 2001. Despite a significant level of capital expenditures, improved earnings attributed to an increase in current taxes payable consistent with an increase in earnings before tax. The Company's current and future tax rate for 2001 was 42.3% versus 44.2% for 2000. As federal and provincial tax rates are expected to drop significantly over the upcoming years, Pason will begin to see the benefit in lower current and, to a lesser extent, future tax.

Net Earnings

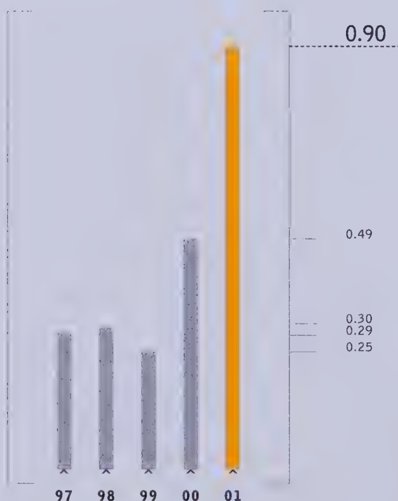
Net earnings increased 90% from $8.1 million or $0.49 per share basic in 2000 to $15.4 million or $0.90 per share basic in 2001. This earnings growth was due to increased revenues in both Canada and the United States as well as new revenues generated in Mexico without a reduction in margins from the prior year.

Cash Flow from Operations

Operating cash flow improved 69% to $24.9 million or $1.45 per share basic in 2001 compared to $14.8 million or $0.89 per share basic recorded a year ago. The majority of this cash flow gain resulted from the $7.3 million increase in earnings and non-cash depreciation totaling $2.0 million. Cash flow was used primarily to finance the Company's 2001 capital expenditure program and improve its year-end working capital position.



NET EARNINGS
($millions)



NET EARNINGS PER SHARE
($basic)

Margins

The margin generated by the Company's rental products increased 1% to 75% while the geological services margin increased 38% to 33% due to concerted efforts to manage the costs of providing the geological services, assisted in part by the new integrated model that includes the TGAS system. The ramp up in rental services infrastructure during the last three years positioned Pason to benefit from the strong industry activity experienced in 2001. The Company, unlike many other service companies, improves its margins not from increased prices, but from an increased number of rental products per site and increasing market share or volume.

Liquidity and Capital Resources

The Company's internal sources of liquidity are cash, short-term investments and cash flow from operations. External sources include the unutilized portion of revolving credit facilities and equipment financings.

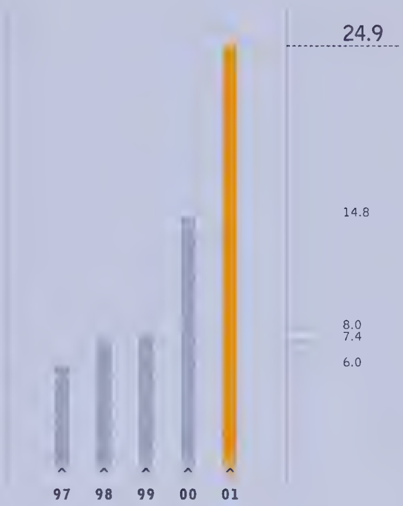
At December 31, 2001, the Company's working capital position was $5.1 million versus $1.4 million at year-end 2000. This $3.7 million or 263% improvement allows for greater financial flexibility in the current uncertain commodity price environment.

Proceeds from the exercise of Company stock options totaled $1.8 million versus $1.0 million in 2000. Approximately $0.1 million was used to reacquire 16,800 Pason common shares for cancellation under the Company's Normal Course Issuer Bid early in 2001. The Normal Course Issuer Bid expired in October 2001 and was not renewed.

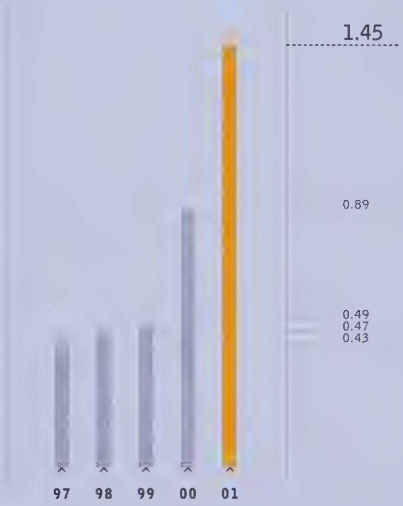
Cash flow and a sales-leaseback financing funded the Company's $22.9 million capital expenditures program, representing a 2% or $0.5 million decrease from the prior year's total expenditure amount of $23.4 million. During 2001, funds were used to acquire and build $21.6 million of new capital assets with a further $1.3 million spent on R&D. Given the weakness in commodity prices and the lower level of drilling activity expected for the first half of 2002, a slow down on capital expenditures was initiated for the 2001 fourth quarter.

At year-end 2001, capital lease obligations amounted to $6.5 million, representing 0.26 times 2001 cash flow compared to 0.76 times a year ago.

The Company's maximum operating line of credit is $5.0 million in Canada and US$1.5 million in the United States.



CASH FLOW
($millions)



CASH FLOW PER SHARE
($basic)

Business Risks

Pason derives its revenue from the rental of instrumentation and data services to oil and gas companies and drilling contractors throughout Canada, the United States and Mexico, and as a result, the major area of uncertainty for Pason is that the demand for its services is directly related to the strength of its clients' capital expenditure programs. The level of capital programs is strongly affected by actual and forecast commodity prices, which can be extremely difficult to predict and beyond the control of Pason and its customers. Weakness in commodity prices could also impact the ability of the Company's customers to pay for the services provided. However, as Pason has a very broad customer base and its services are a minor component when looking at the overall cost of drilling a well, the risk is minimal.

Pason carries adequate levels of insurance to protect the Company. Due to the wide geographical distribution of equipment throughout North America, the possibility of a loss to a significant portion of its asset base is extremely unlikely. As the Company's equipment is largely unmanned, the customer assumes responsibility for its maintenance and performance.

The Company does not employ hazardous materials, so the possibility of environmental liabilities is limited.

Merger and acquisition activity in the oil and gas exploration and production sector may impact demand for the Company's services, as customers tend to focus on reorganization activities prior to committing funds to major drilling programs. Pason is also subject to risks and uncertainties associated with weather and seasonality. Pason continues to react to unfavourable weather conditions and spring breakup through diversification into geographic regions such as the United States and Mexico where these factors are less likely to influence activity.

Outlook

As commodity price uncertainty continues, significant concern exists with the supply and demand fundamentals for crude oil and natural gas. Throughout the latter half of 2001, the reduction in oil and gas prices put pressure on the industry to reduce its drilling activity, and despite this pressure, 2001 was a year of strong activity with over 18,000 wells drilled. The Company continues to be well positioned to profit from the high levels of oilfield activity and increased market share, and expects to spend in excess of $20.0 million during 2002 to add supplementary products in Canada, and to a greater extent in the United States and Mexico where significant room for additional market share exists. The Company will continue to pursue other international opportunities that fall within its service parameters.

Pason made a significant investment over the past several years to develop an infrastructure that supported the oil and gas industry's 2001 activity levels. During 2001, the Company's focus was to maximize the relationship between operating efficiencies, operating costs and customer service and this focus will continue into 2002 in a more sensitive operating environment.

Management's Report

To the Shareholders of Pason Systems Inc.

The accompanying consolidated financial statements are the responsibility of management and have been approved by the Board of Directors of the Company. Management is responsible for and has prepared and presented the consolidated financial statements in accordance with Canadian generally accepted accounting principles and has made significant accounting judgements and estimates as required. Management has ensured that financial information contained elsewhere in this Annual Report is consistent with the consolidated financial statements.

The Board of Directors is responsible for reviewing and approving the consolidated financial statements and ensuring management meets their financial reporting responsibilities.

JD Hill

JAMES D. HILL
PRESIDENT & CHIEF EXECUTIVE OFFICER

J Dickie

JOANNE DICKIE
CHIEF FINANCIAL OFFICER

Calgary, Alberta
March 11, 2002

Auditors' Report

To the Shareholders of Pason Systems Inc.

We have audited the consolidated balance sheets of Pason Systems Inc. as at December 31, 2001 and 2000 and the consolidated statements of earnings and retained earnings and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2001 and 2000 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

Deloitte & Touche LLP

CHARTERED ACCOUNTANTS

Calgary, Alberta
February 22, 2002

December 31,	2001	2000
	$	$
ASSETS		
Current		
Cash and term deposits	**1,253,713**	1,441,426
Accounts receivable	**14,986,321**	13,992,704
Inventory	**3,592,319**	2,463,784
Prepaid expenses	**443,256**	251,691
	20,275,609	18,149,605
Capital assets [Note 5]	**58,653,315**	43,324,782
Deferred development costs [Note 6]	**2,820,290**	2,352,396
Goodwill [Note 7]	**503,058**	624,195
	82,252,272	64,450,978
LIABILITIES		
Current		
Bank indebtedness [Note 8]	**2,610,000**	1,590,000
Accounts payable and accrued liabilities	**6,192,477**	7,962,119
Income taxes payable	**2,840,873**	3,606,912
Current portion of long-term debt [Note 9]	**278,525**	262,652
Current portion of obligations under capital leases [Note 10]	**3,219,003**	3,312,094
	15,140,878	16,733,777
Long-term debt [Note 9]	**394,527**	634,694
Obligations under capital leases [Note 10]	**6,491,392**	7,834,379
Future income taxes [Note 12]	**6,284,059**	3,799,834
	28,310,856	29,002,684
SHAREHOLDERS' EQUITY		
Share capital [Note 11]	**14,045,635**	12,266,526
Foreign currency translation adjustment	**2,105,033**	732,399
Retained earnings	**37,790,748**	22,449,369
	53,941,416	35,448,294
	82,252,272	64,450,978

Approved by the Board of Directors

JAMES D. HILL
DIRECTOR

JAMES B. HOWE
DIRECTOR

Years Ended December 31,	2001	2000
	$	$
Revenue		
Drilling recorder rentals	**31,795,631**	21,058,225
Pit volume totalizer rentals	**17,316,714**	12,405,340
Geological services	**9,403,774**	7,045,113
Choke control rentals	**1,292,090**	538,181
Total gas rentals	**1,105,317**	–
Other income	**2,102,598**	1,097,311
	63,016,124	42,144,170
Expenses		
Rental services	**13,641,302**	9,289,546
Geological services	**6,261,824**	5,326,028
Shop	**2,551,586**	1,899,549
Research and development	**2,750,333**	2,006,024
Administration	**2,414,706**	2,825,782
Interest on long-term obligations	**1,075,672**	762,225
Interest – other	**248,011**	153,284
Depreciation and amortization	**7,341,047**	5,339,644
	36,284,481	27,602,082
Earnings from operations before income taxes	**26,731,643**	14,542,088
Income taxes [Note 12]		
Current	**9,131,759**	5,085,077
Future	**2,162,597**	1,339,616
	11,294,356	6,424,693
Net earnings	**15,437,287**	8,117,395
Retained earnings, beginning of year	**22,449,369**	14,875,233
Change in accounting policy [Note 4]	–	(435,955)
Repurchase of common shares [Note 11]	**(95,908)**	(107,304)
Retained earnings, end of year	**37,790,748**	22,449,369
Earnings per share [Note 14]		
Basic	**0.90**	0.49
Diluted	**0.88**	0.47

Years Ended December 31,	2001	2000
	$	$
Cash flows related to the following activities:		
Operating		
Net earnings	**15,437,287**	8,117,395
Adjustments for:		
Depreciation and amortization	**7,341,047**	5,339,644
Future income taxes	**2,162,597**	1,339,616
Cash flow from operations	**24,940,931**	14,796,655
Changes in non-cash working capital	**(4,849,399)**	1,169,808
	20,091,532	15,966,463
Financing		
Issue of common shares	**1,797,421**	970,868
Repurchase of common shares under Normal Course Issuer Bid [Note 11]	**(114,220)**	(125,700)
Proceeds from long-term debt, net of repayments	**(224,294)**	897,346
Proceeds from capital leases, net of repayments	**(1,436,078)**	6,048,015
	22,829	7,790,529
Investing		
Purchase of capital assets	**(21,589,629)**	(21,680,089)
Development costs	**(1,331,864)**	(1,739,324)
Proceeds on disposal of capital assets	**226,785**	375,510
	(22,694,708)	(23,043,903)
Foreign currency translation adjustment	**1,372,634**	660,847
Net (decrease) increase in cash and cash equivalents	**(1,207,713)**	1,373,936
Cash and cash equivalents, beginning of year	**(148,574)**	(1,522,510)
Cash and cash equivalents, end of year	**(1,356,287)**	(148,574)
Represented by:		
Cash and term deposits	**1,253,713**	1,441,426
Bank indebtedness	**(2,610,000)**	(1,590,000)
	(1,356,287)	(148,574)
Cash flow per share [Note 14]		
Basic	**1.45**	0.89
Diluted	**1.42**	0.85

Supplemental cash flow information [Note 16]

Years Ended December 31, 2001 and 2000

1. Description of Business

Pason Systems Inc. (the "Company") designs and manufactures for rent specialized proprietary instrumentation for use on land-based drilling rigs.

2. Basis of Presentation

The accompanying consolidated financial statements include the accounts of Pason Systems Inc. and its wholly owned subsidiaries Pason Systems Corp., Pason Systems USA Corp. and Pason de Mexico S.A. de C.V.

Certain comparative figures have been reclassified to conform to the current year presentation.

3. Change in Accounting Policy

Effective January 1, 2001, the Company adopted retroactively the new accounting recommendation of the Canadian Institute of Chartered Accountants for calculating earnings per share. The new standard requires the use of the treasury stock method for calculating diluted earnings per share. The 2000 comparative figures have been recalculated under the new method and remain unchanged.

4. Significant Accounting Policies

INVENTORY

Inventory is comprised of parts and raw materials awaiting assembly into capital assets. Inventory is recorded at the lower of average cost and net realizable value.

CAPITAL ASSETS

The electronic drilling recorders and pit volume totalizer systems are recorded at cost and are depreciated using a unit-of-use method based on 1,800 rental days with a 10% salvage or residual value.

All other capital assets are recorded at cost and are depreciated using the declining-balance method at the following annual rates:

Geological services equipment	10%
Drilling choke controls	20%
Trucks	30%
Other	30%

Leasehold improvements are amortized on a straight-line basis over the terms of the leases, which range from two to ten years.

RESEARCH AND DEVELOPMENT

The Company follows the practice of expensing all research expenditures as incurred, net of related investment tax credits. Development costs are expensed as incurred, unless they meet the criteria for deferral and amortization under Canadian generally accepted accounting principles.

Development costs incurred on new product development projects, which, in the Company's view, have clearly defined market prospects are deferred and are amortized over three years commencing in the year in which the new products begin generating rental revenue. However, at such time that the products are deemed not commercially viable, the balance of the related costs will be expensed.

FOREIGN CURRENCY TRANSLATION

The accounts of the Company's self-sustaining foreign operations are translated into Canadian dollars using the current-rate method. Assets and liabilities are translated at the year-end exchange rate and revenues and expenses are translated at average exchange rates. Gains and losses arising from the translation of the financial statements of the foreign operations are deferred in a foreign currency translation adjustment account in shareholders' equity.

4. Significant Accounting Policies (continued)

GOODWILL

Goodwill is recorded at cost and is being amortized on a straight-line basis over a period of ten years. The recoverability of goodwill is assessed annually based on the estimated future cash flows related to operations in the United States.

INCOME TAXES

The Company follows the liability method of accounting for income taxes. Under this method, the Company records future income taxes on the effect of any differences between the accounting and income tax basis of an asset or liability. The effect of a change in income tax rates on future income tax liabilities is recognized in income in the period that the change occurs.

Effective January 1, 2000, the Company adopted the new accounting recommendation of the Canadian Institute of Chartered Accountants for accounting for income taxes using the liability method. The new policy was applied retroactively that resulted in a decrease in opening retained earnings of $435,955 for 2000, representing the cumulative effect of the change on prior years.

USE OF ESTIMATES

The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenue and expenses during the reporting period. The most significant of these estimates are related to the provision of doubtful accounts receivable and the amortization period for fixed assets and goodwill. Actual results could differ significantly from these estimates.

5. Capital Assets

			2001
	Cost	Accumulated Depreciation and Amortization	Net Book Value
	$	$	$
Electronic drilling recorders	**35,434,520**	**4,419,204**	**31,015,316**
Electronic drilling recorders under capital lease	**10,296,792**	**1,284,160**	**9,012,632**
Pit volume totalizers	**8,253,116**	**1,948,125**	**6,304,991**
Pit volume totalizers under capital lease	**2,185,160**	**515,801**	**1,669,359**
Total gas systems	**2,168,807**	**–**	**2,168,807**
Geological services equipment	**4,739,025**	**2,805,245**	**1,933,780**
Electronic drilling choke controls	**1,673,576**	**458,263**	**1,215,313**
Trucks	**1,868,744**	**1,016,447**	**852,297**
Trucks under capital lease	**1,721,700**	**1,084,984**	**636,716**
Leasehold improvements	**2,914,117**	**954,889**	**1,959,228**
Other	**3,593,877**	**1,709,001**	**1,884,876**
	74,849,434	**16,196,119**	**58,653,315**

5. Capital Assets (continued)

			2000
	Cost	Accumulated Depreciation and Amortization	Net Book Value
	$	$	$
Electronic drilling recorders	20,687,245	2,902,987	17,784,258
Electronic drilling recorders under capital lease	12,014,226	1,912,564	10,101,662
Pit volume totalizers	6,141,839	1,533,645	4,608,194
Pit volume totalizers under capital lease	1,050,000	287,605	762,395
Total gas systems	135,010	–	135,010
Geological services equipment	4,303,089	1,600,704	2,702,385
Electronic drilling choke controls	985,401	461,392	524,009
Trucks	1,996,784	837,469	1,159,315
Trucks under capital lease	1,939,954	743,769	1,196,185
Leasehold improvements	2,774,645	625,306	2,149,339
Other	3,209,897	1,007,867	2,202,030
	55,238,090	11,913,308	43,324,782

The depreciation recorded in 2001 is $6,477,077 (2000 – $5,078,537).

6. Deferred Development Costs

	2001	2000
	$	$
Balance, beginning of year	**2,613,503**	874,179
Additional costs deferred	**1,331,864**	1,739,324
	3,945,367	2,613,503
Amortization	**(1,125,077)**	(261,107)
Balance, end of year	**2,820,290**	2,352,396

The amortization recorded in 2001 is $863,970 (2000 – $261,107).

7. Goodwill

			2001	2000
	Cost	Accumulated Amortization	Net Book Value	Net Book Value
	$	$	$	$
Goodwill	**1,261,133**	**(758,075)**	**503,058**	624,195

The amortization recorded in 2001 is $154,815 (2000 – $165,391).

8. Bank Indebtedness

The Company's subsidiary, Pason Systems Corp., has a $5,000,000 credit facility, which bears interest at the bank prime rate plus 0.75%. A general assignment of its accounts receivable is pledged as collateral. At December 31, 2001, an amount of $2,610,000 had been drawn on this credit facility (2000 – $1,590,000).

8. Bank Indebtedness (continued)

The Company's U.S. subsidiary has a US$1,500,000 (CDN$2,387,250) revolving line of credit, which bears interest at bank prime rate plus 0.5%. The revolving line of credit requires monthly interest payments and matures July 31, 2002. At December 31, 2001, no amount was drawn on the line of credit. A general assignment of its accounts receivable, equipment and inventory is pledged as collateral.

In 2000, the Company's U.S. subsidiary had a US$500,000 (CDN$750,400) revolving line of credit with interest at bank prime rate plus 0.5%. At December 31, 2000, no amount had been drawn on this credit facility.

9. Long-Term Debt

The Company's U.S. subsidiary has a US$700,000 (CDN$1,036,560) term facility at prime rate plus 0.5% and requires monthly principal payments of US$14,584 (CDN$23,210) plus interest to May 20, 2004. A general assignment of its accounts receivable, equipment and inventory is pledged as collateral. At December 31, 2001, US$422,904 (CDN$673,052) (2000 – US$597,912 (CDN$897,346)) was outstanding on the term facility. The current portion as at December 31, 2001 was US$175,008 (CDN$278,525).

10. Obligations Under Capital Leases

Future minimum payments under capital leases as at December 31, 2001 and 2000 are as follows:

	2001	2000
	$	$
2001	–	4,144,596
2002	**4,075,647**	3,315,798
2003	**4,043,625**	3,262,940
2004	**2,772,645**	2,211,705
	10,891,917	12,935,039
Effective interest on leases at 7% to 9%	**1,181,522**	1,788,566
	9,710,395	11,146,473
Less current portion	**3,219,003**	3,312,094
	6,491,392	7,834,379

11. Share Capital

Authorized
Unlimited number of common shares
Unlimited number of preferred shares

Issued
Common shares

	Shares	Amount
	#	$
Balance, December 31, 1999	16,295,721	**11,314,054**
Exercise of employee stock options	509,165	**970,868**
Purchased and cancelled [Note 11(b)]	(15,900)	**(18,396)**
Balance, December 31, 2000	16,788,986	**12,266,526**
Exercise of employee stock options	663,843	**1,797,421**
Purchased and cancelled [Note 11(b)]	(16,800)	**(18,312)**
Balance, December 31, 2001	17,436,029	**14,045,635**

11. Share Capital (continued)

a) At December 31, 2001, stock options were outstanding for 1,872,142 common shares at $2.10 to $10.10 per share expiring between April 7, 2002 and December 30, 2006 as follows:

	2001		2000	
	Share Options	Weighted Average Exercise Price	Share Options	Weighted Average Exercise Price
	#	$	#	$
Outstanding, beginning of year	**1,962,135**	**4.83**	1,875,000	3.64
Granted	**878,250**	**7.74**	806,800	7.08
Exercised	**(663,843)**	**2.71**	(509,165)	1.91
Cancelled	**(304,400)**	**6.66**	(210,500)	5.95
Outstanding, end of year	**1,872,142**	**6.63**	1,962,135	4.83
Exercisable, end of year	**630,742**		821,635	
Available for grant, end of year	**220,181**		52,543	

	2001		2000	
Range of Exercise Price	Options Outstanding	Weighted Average Exercise Price	Options Outstanding	Weighted Average Exercise Price
	#	$	#	$
$0.70 – $4.00	**296,900**	**3.13**	770,743	2.20
$4.01 – $6.50	**426,392**	**6.26**	769,892	5.92
$6.51 – $10.10	**1,148,850**	**7.68**	421,500	7.66
	1,872,142	**6.63**	1,962,135	4.83

b) Effective October 2, 2000, The Toronto Stock Exchange accepted notice of the Company's intention to make a Normal Course Issuer Bid (the "Bid") through the facilities of the exchange. The Bid commenced on October 4, 2000 and expired on October 3, 2001. Under the provisions of the Bid, the Company purchased 16,800 (2000 – 15,900) common shares during 2001 at an average price of $6.80 (2000 – $7.93) per share. The shares have subsequently been cancelled. The cost of the purchases was $114,220 (2000 – $125,700) of which $18,312 (2000 – $18,396) was charged to share capital based on the average book value per share as of the date of purchase, and the remaining $95,908 (2000 – $107,304) was charged to retained earnings.

12. Income Taxes

The provision for income taxes reflects an effective income tax rate, which differs from the combined federal and provincial statutory rates of 41.6% for 2001 and 43.6% for 2000. As well, Pason Systems USA Corp. has federal and state statutory tax rates of 40% for 2001 and 2000. The main differences are as follows:

	2001	2000
	$	$
Earnings before income taxes	**26,731,643**	14,542,088
Expected income taxes	**11,125,709**	6,430,350
Increase (decrease) resulting from:		
Temporary differences related to the sale of intercompany capital assets	**763,094**	477,757
Share issuance deductions	**(62,095)**	(77,773)
Other non deductibles	**60,135**	27,548
Lower foreign income tax rates	**(293,144)**	(157,533)
Recognized benefit of losses	**(299,343)**	(275,656)
Income tax expense	**11,294,356**	6,424,693

The Company has future income tax assets and liabilities as follows:

	2001	2000
	$	$
Temporary differences related to capital assets	**(6,284,059)**	(3,865,168)
Future tax benefit of share issuance costs	–	65,334
	(6,284,059)	(3,799,834)

13. Financial Instruments

The fair value of financial instruments, which include accounts receivable, inventory, bank indebtedness, accounts payable and accrued liabilities, long-term debt and obligations under capital leases approximates amounts at which these instruments could be exchanged in a transaction between knowledgeable and willing parties.

The Company is exposed to credit risk to the extent that its customers may experience financial difficulty and would be unable to meet their obligations. However, the Company has a large number of customers, which minimizes concentration of credit risk.

Obligations under capital leases carry interest at rates which are not significantly different from year-end interest rates. Consequently, the fair value of these long-term liabilities approximates their carrying value.

Long-term debt is based on prime rate interest rates. As a result of fluctuations to prime rates, the Company is exposed to interest rate risks.

14. Per Share Amounts

Earnings and cash flow per share have been calculated using the weighted average number of common shares outstanding during the year, which amounted to 17,147,210 shares (2000 – 16,603,965). Diluted amounts per share have been calculated using the weighted average number of common shares of 17,539,062 (2000 – 17,320,136).

15. Segmented Information

				2001
	Canada	U.S.	Mexico	Total
	$	$	$	$
Revenue from external customers	**35,884,490**	**26,744,745**	**386,889**	**63,016,124**
Depreciation and amortization	**4,699,302**	**2,628,372**	**13,373**	**7,341,047**
Operating costs	**13,397,763**	**14,034,536**	**13,189**	**27,445,488**
Segment operation profit	**17,787,425**	**10,081,837**	**360,327**	**28,229,589**
Interest on long-term obligations				**1,075,672**
Interest – other				**248,011**
Corporate expenses				**174,263**
Income tax expense				**11,294,356**
Net earnings				**15,437,287**
Identifiable assets	**52,399,941**	**28,778,527**	**1,073,804**	**82,252,272**
Capital expenditures	**10,875,620**	**10,109,614**	**604,395**	**21,589,629**

			2000
	Canada	U.S.	Total
	$	$	$
Revenue from external customers	28,058,660	14,085,510	42,144,170
Depreciation and amortization	3,720,424	1,619,220	5,339,644
Operating costs	10,677,665	10,497,117	21,174,782
Segment operation profit	13,660,571	1,969,173	15,629,744
Interest on long-term obligations			762,225
Interest – other			153,284
Corporate expenses			172,147
Income tax expense			6,424,693
Net earnings			8,117,395
Identifiable assets	46,094,984	18,355,994	64,450,978
Capital expenditures	16,327,187	5,352,902	21,680,089

16. Supplemental Cash Flow Information

Interest paid during 2001 was $1,323,683 (2000 – $915,509). Income tax paid during 2001 was $9,836,512 (2000 – $1,899,299).

17. Commitments

The Company entered into leases for office premises commencing on various dates in 2000 and 2001 and expiring May 31, 2010 with an option for an additional five (5) years. The Calgary minimum annual rental payments in years two through five are $557,314 and $659,468 in year six. Minimum annual lease payments of $122,585 to September 30, 2004 are required under the Company's Denver lease and minimum average annual lease payments of $74,000 to December 31, 2006 are required under the Company's Houston lease.

The Company entered into operating leases for its new vehicles commencing January 2001 with minimum annual rental payments in 2002 – $541,800; 2003 – $565,900 and 2004 – $367,200.

Selected Financial Data

Years Ended December 31,	2001	2000	1999	1998	1997	1996
(000s, except per share amounts)	$	$	$	$	$	$
Operating Results						
Revenue	**63,016**	42,144	24,668	23,768	14,496	4,497
Expenses						
Rental services	**13,641**	9,290	5,649	4,830	2,348	1,029
Geological services	**6,262**	5,326	3,852	3,568	911	–
Shop	**2,551**	1,900	1,426	1,125	740	298
Administration	**2,415**	2,826	1,867	1,631	702	441
Research & development	**2,750**	2,006	1,403	967	508	222
Depreciation & amortization	**7,341**	5,340	2,898	2,584	1,689	580
Net earnings	**15,437**	8,117	4,084	4,900	4,102	909
Per share – basic	**0.90**	0.49	0.25	0.30	0.29	0.07
Cash flow from operations	**24,941**	14,797	7,966	7,417	6,014	1,537
Per share – basic	**1.45**	0.89	0.49	0.47	0.43	0.11
EBITDA	**35,396**	20,797	10,511	11,686	9,275	2,332
Per share – basic	**2.06**	1.25	0.65	0.73	0.66	0.19
Capital expenditures	**22,921**	23,419	10,851	8,294	7,957	2,438
Financial Position						
Current assets	**20,276**	18,150	11,461	10,470	10,529	3,028
Total assets	**82,252**	64,451	40,193	30,736	25,179	7,346
Working capital	**5,135**	1,416	3,283	5,769	3,824	600
Long-term debt	**395**	635	–	–	233	364
Future income tax	**6,284**	3,800	2,159	1,030	860	81
Shareholders' equity	**53,941**	35,448	26,261	22,639	16,878	3,979
Return on shareholders' equity	**35%**	26%	17%	24%	41%	43%
Common Share Data						
Common shares outstanding (#)						
At December 31	**17,436**	16,789	16,296	16,169	15,900	13,721
Weighted average	**17,147**	16,604	16,257	16,103	14,058	12,412
Share trading						
High ($)	**10.34**	9.75	6.90	8.50	6.50	2.40
Low ($)	**6.00**	5.50	2.25	2.50	6.30	0.70
Close ($)	**9.10**	6.95	6.25	2.90	6.50	2.15
Volume (#)	**4,423**	3,233	3,266	4,987	4,422	n/a

DIRECTORS

Harold R. Allsopp (1)(2)
President
Habede Holdings Ltd.
Calgary, Alberta

Murray L. Cobbe (2)(3)
President
Trican Well Service Ltd.
Calgary, Alberta

James D. Hill (1)
President & Chief Executive Officer
Pason Systems Inc.
Calgary, Alberta

James B. Howe (1)(2)
President
Bragg Creek Investments Ltd.
Calgary, Alberta

Paul F. Little (3)
Private Investor, Corporate Director,
Financial Adviser
Calgary, Alberta

Peter S. Mackechnie (3)
Associate Director
Bear Stearns
Los Angeles, California

(1) Audit Committee Member
(2) Compensation Committee Member
(3) Corporate Governance Committee Member

OFFICERS AND KEY PERSONNEL

Pason Systems Inc.

Jim Hill
President & Chief Executive Officer

Joanne Dickie
Chief Financial Officer

Pason Systems Corp.

Jim Hill
President

Joanne Dickie
Chief Financial Officer

Lucy Tomie
Controller

Bob Rodda
Canadian Business Unit Manager

David White
Field Products Project Manager

Robert Kenny
Office Products Project Manager

Francis Dunlop
Technical Manager

James Parks
Manufacturing Manager

Pason Systems USA Corp.

Jim Hill
President

Ben Thomas
US Business Unit Manager

Jerry Aberle
Chief Financial Officer

Art Curtis
Geological Operations Manager

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Calgary, Alberta T2P 0S2
Telephone: (403) 233-2801

STOCK TRADING

Toronto Stock Exchange
Trading Symbol: PSI

ANNUAL MEETING

The Annual Meeting of Shareholders of Pason Systems Inc. will be held on Monday, June 3, 2002 at 3:30 p.m. (Calgary time) in the offices of Pason Systems Inc., 6130 Third Street S.E., Calgary, Alberta. Shareholders who are unable to attend the Meeting are requested to complete and return the Instrument of Proxy to Valiant Trust Company at their earliest convenience.

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